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Acronyms

DRMO
DRMS

Defense Reutilization and Marketing Office
Defense Reutilization and Marketing Service

Evaluation



Report

OFFICE OF THE INSPECTOR GENERAL

**EVALUATION REPORT OF DEFENSE HOTLINE
ALLEGATIONS ON IMPROPER SALE AND
DISPOSAL OF DOD PALLETS**

Report No. 97-190

July 17, 1997

DEPARTMENT OF DEFENSE

AQI 00-01-0059



**INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-2884**



July 17, 1997

**MEMORANDUM FOR DEPUTY UNDER SECRETARY OF DEFENSE
(ENVIRONMENTAL SECURITY)
ASSISTANT SECRETARY OF THE NAVY (FINANCIAL
MANAGEMENT AND COMPTROLLER)
AUDITOR GENERAL, DEPARTMENT OF THE ARMY**

**SUBJECT: Evaluation Report of Defense Hotline Allegations on Improper Sale and
Disposal of DoD Pallets (Report No. 97-190)**

We are providing this report for your information and use. We provided a draft of this report to you on June 2, 1997. Because the report contains no findings or recommendations, written comments were not required and none were received. Therefore, we are publishing this report in final form.

We appreciate the courtesies extended to the evaluation staff. Questions on the evaluation should be directed to Ms. Debra B.D. Murphy, Evaluation Program Director, at (703) 604-8788 (DSN 664-8788) or Colonel (Select) Martin J. Sierocki, U. S. Air Force, Evaluation Project Manager, at (703) 604-8766 (DSN 664-8766). See Appendix C for the report distribution. The evaluation team members are listed inside the back cover.

Robert J. Lieberman
Assistant Inspector General
for Auditing

Office of the Inspector General, DoD

Report No. 97-190

(Project No. 7LH-8008)

July 17, 1997

**Defense Hotline Allegations on Improper Sale and Disposal of
DoD Pallets**

Executive Summary

Introduction. The evaluation was conducted in response to allegations made to the Defense Hotline. Specifically, it was alleged that several Defense installations in the southeastern United States (Jacksonville Naval Air Station, Florida; Mayport Naval Station, Florida; Kings Bay Naval Base, Georgia; and Fort Stewart, Georgia) were not recycling pallets through Defense Reutilization and Marketing Offices; inappropriately selling excess pallets; and improperly distributing cash proceeds to Morale, Welfare and Recreation accounts.

Evaluation Objective. The objective of the evaluation was to determine the validity of the allegations. We also evaluated the management control program as it related to the primary evaluation objective.

Evaluation Results. Managers at the four installations appropriately recycled, sold, and transferred cash proceeds to their respective Morale, Welfare, and Recreation account from the sale of excess wooden pallets. Specifically, all four installations sold pallets through their recycling center as authorized. None of the four installations were using the Defense Reutilization and Marketing Office for pallet recycling because Headquarters, Defense Reutilization and Marketing Service policy is to not recycle damaged pallets, which its managers considered refuse. In addition, all four installations had appropriately transferred proceeds from pallet sales to their respective Morale, Welfare, and Recreation account. The management controls reviewed were adequate in that we identified no material management control weaknesses.

Management Comments. Because this report contains no findings or recommendations, written comments were not required and none were received. Therefore, we are publishing this report in final form.

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Part I - Evaluation Results

Evaluation Background

Defense Hotline Allegations. The evaluation was conducted in response to allegations made to the Defense Hotline. Specifically, it was alleged that several Defense installations in the southeastern United States (Jacksonville Naval Air Station, Florida; Mayport Naval Station, Florida; Kings Bay Naval Base, Georgia; and Fort Stewart, Georgia) were not recycling pallets through Defense Reutilization and Marketing Offices (DRMO); inappropriately selling excess pallets; and improperly distributing cash proceeds.

Pallets Used for Efficient Transportation. Pallets are used as transport platforms to ease and speed the movement of supplies and equipment. Forklifts are used to transport pallets and their associated commodity. The most commonly used DoD pallet is made of wood and costs \$8.25. The DoD supply system has 18 national stock numbers for pallets in inventory, and purchased approximately \$10 million of pallets during FY 1996. However, DoD receives most of its pallets from vendors as a by-product of the delivery process.

Legislative and Executive Order Basis for Recycling. United States Code, title 10, section 2577 (10 U.S.C. 2577), "Disposal of Recyclable Materials," provides the legislative basis for the sale of DoD recyclable material. Under the provisions of section 2577, paragraphs (b)(1); (b)(2); and (b)(3), the law indicates that after program costs are recovered, installations may use up to 50 percent of the net proceeds from the sale of recyclable material for various environmental or health and safety purposes or the net proceeds may go towards Morale, Welfare, and Recreation programs. Executive Order 12873, "Federal Acquisition, Recycling, and Waste Prevention," October 20, 1993, (which superseded Executive Order 12780, October 31, 1991) requires that each Executive agency initiate a program to promote cost-effective waste reduction and recycling of reusable materials in all of its facilities.

Federal and DoD Guidance. The Deputy Under Secretary of Defense (Environmental Security) implemented 10 U.S.C. 2577 and the requirements of Executive Orders 12780 and 12873 through a policy memorandum issued in September 1993. The Defense Logistics Agency, through the Defense Reutilization and Marketing Service (DRMS), was the primary agency responsible for the sale of recyclable material. Upon request and approval by the Defense Logistics Agency, an installation could obtain authorization by waiver to directly sell recyclable material. The policy memorandum was superseded by DoD Instruction 4715.4, "Pollution Prevention," June 18, 1996, which implements policy, assigns installation responsibilities, and prescribes procedures for

implementation of pollution prevention programs throughout DoD. The instruction requires the heads of the Military Departments, the Defense agencies, and the DoD field organizations to establish cost-effective recycling programs and publish procedures that authorize installation commanders to sell recyclable material directly or consign the material to the DRMS for sale, without DLA approval.

Combined Service Guidance. On January 1, 1997, a combined Services memorandum, "Interim Guidance for Direct Sales" was published. The memorandum granted installation commanders the authority to directly sell recyclable commodities, such as scrap wood in unserviceable pallets, without going through the Defense Logistics Agency or the DRMS. In addition, a combined Services qualified recycling program guide is being developed that will contain detailed guidance for managing and operating a direct sales program. The guide is planned for release by the end of FY 1997.

Evaluation Objectives

The objective of this evaluation was to determine the validity of allegations received from the Defense Hotline concerning improper disposal, sale, and distribution of wooden pallet proceeds at four Defense installations. Specifically, we sought to determine whether:

- o installations were recycling pallets through DRMOs,
- o installations were selling pallets without authorization to sell recyclable material, and
- o cash proceeds were being distributed to the installations' Morale, Welfare, and Recreation accounts without authorization.

See Appendix A for a discussion of the evaluation scope and methodology and for the results of the review of the management control program. Appendix B discusses the specific allegations and our evaluation results pertaining to each allegation.

Implementation of DoD Recycling Policy

The four Defense installations appropriately obtained, recycled, and sold excess wooden pallets. In addition, the cash proceeds from the sale of pallets were properly distributed. Appropriate recycling, sales, and distribution of cash proceeds occurred because the installations had properly implemented DoD recycling policies and regulations. As a result, the installations were in compliance with prevailing DoD recycling policy and regulations associated with the management of recyclable material.

Obtaining Pallets

The four installations reviewed appropriately obtained standard wooden pallets as either by-products of items purchased through the supply system, or from installations undergoing base realignments and closures. Unique or non-standard pallets were obtained by issuing purchase orders using assigned national stock numbers.

Pallets Obtained as By-Products of Purchased Materials. Before the 1990s, the most common way a DoD installation obtained pallets was by ordering them through the supply system using an assigned national stock number. However, in the early 1990s, the way DoD received most of its pallets changed. The trucking industry uses palletization as its primary method of moving vast amounts of supplies and materials. Specifically, pallets became a by-product of supplies and materials acquired through DoD purchase orders and contracts. As a consequence, every pallet located on a DoD installation was not purchased through the DoD supply system. More likely, an industry standard 48x40-inch wooden pallet was received in conjunction with a purchased item. Pallets are considered part of the shipping and handling aspects of the trucking industry, and normally are not accounted for or recycled.

Pallets Obtained Through Base Realignment and Closure. The three Navy installations reviewed obtained pallets from nearby DoD installations undergoing base realignment and closure. For FYs 1995 and 1996, those installations collectively acquired 7,980 pallets by that method, saving the installations an estimated \$66,000 (less transportation costs) had new pallets been purchased. Ft. Stewart had not obtained any pallets through base realignments and closures because it obtained pallets as by-products of purchased materials.

Pallets Obtained Through the Supply System. Of the four installations visited, only Jacksonville Naval Air Station had ordered new pallets. Although it ordered no pallets for FY 1997, Jacksonville ordered 17,800 pallets for FYs 1995 and 1996 at an estimated cost of \$147,000. The pallets ordered were specifically designed for hoisting cargo onto ships and were a different design than the industry standard 48x40-inch wooden pallet obtained as by-products of purchased materials.

Recycling Pallets

Each of the four installations visited appropriately recycled excess wooden pallets at its installation in an efficient manner through its recycling program. The DRMOs visited did not recycle pallets.

Installation Recycling of Pallets. The four installations appropriately recycled excess wooden pallets through their local recycling programs. One installation, Kings Bay Naval Base, demonstrated exceptional innovation and made pallet recycling cost-effective for its installation. We considered it a best practice model. Five interrelated initiatives enabled Kings Bay to make pallet recycling cost-effective. First, Kings Bay obtained 5,280 excess pallets at no cost, other than transportation costs, from nearby installations closed through base realignment and closure. Those pallets were acquired from the beginning of FY 1995 through the first quarter of FY 1997. Obtaining pallets from base realignment and closure installations saved Kings Bay \$43,500 in pallet purchases. Second, Kings Bay created a pallet recycling program that required base personnel with excess pallets to contact the recycling center for pickup. The recycling center sent a truck to pick up the excess, and if the pallets were in reusable condition, the truck delivered the pallets to a central staging area for reuse by the Fleet Industrial Supply Center. The quantity of pallets recycled at the Fleet Industrial Supply Center was annotated and the weight of the recycled pallets was claimed as a landfill cost avoidance on the Kings Bay Annual Solid Waste Report. During FYs 1995 through 1997, 10,800 pallets were recycled with an associated landfill cost avoidance of approximately \$22,400. Third, at the weigh-in station of the landfill, trucks were visually inspected, and if recyclable pallets were observed, the truck was not permitted to unload but instead directed to first offload the pallets at the recycling center. Fourth, the Fleet Industrial Supply Center contracted with a local company to pick up, transport, refurbish, and return the refurbished pallets to the Fleet Industrial Supply Center at a price of \$2.50 per pallet versus the \$8.25 cost for a new pallet. Of the four installations visited, Kings Bay was the only installation with a pallet rebuild contract. If a pallet was in a condition beyond

refurbishment it was sold as wooden scrap, which generated revenue for Kings Bay. Fifth, Kings Bay published a quarterly circular, "Plan of the Week" to all units. It contains recycling information, points of contact, and telephone numbers for base recycling and encourages participation in the Kings Bay recycling program.

DRMO Recycling of Pallets. At each of the four installations visited, a DRMO collocated with the installation was also visited. None of the four DRMO managers recycled pallets. Specifically, DRMO managers stated that excess pallets were considered disposable refuse because in most cases, the pallets they received were damaged with broken slats or headers. To determine whether DRMOs were actually receiving damaged pallets, we inspected approximately 10 percent of the pallets at each of the four DRMOs visited. In most cases, the pallets were damaged and would require extensive work to make them serviceable. In addition, managers stated that they did not have available manpower, tools, or the time needed to rebuild pallets in a cost-effective manner. Further, none of the 18 national stock numbers assigned to DoD pallets were ordered by the DRMOs. The DRMOs were not storing pallets, other than the mostly damaged pallets, that had equipment or supplies affixed to them. Because the four DRMOs received mostly damaged or unserviceable pallets, and had limited space to store them, it was impractical for the DRMOs to offer serviceable pallets for reutilization, transfer, or donation.

Sale of Excess Pallets

Direct Sales and Recycling Programs. The four installations visited appropriately and efficiently sold excess wooden pallets by using their direct sales authority. While the primary focus of recycling is to reduce the waste stream, conserve natural resources, and prevent pollution at DoD installations, a key aspect of effective recycling is to minimize costs, such as the costs associated with trash hauling and disposal.

Cost-Avoidance Through Recycling. A major benefit of recycling pallets is the costs saved by avoiding transportation and landfill disposal costs. Specifically, landfill tipping fees, as well as transportation costs are avoided when pallets are recycled. Installations are charged a tipping fee for every ton of refuse sent to a commercial or local government landfill. The tipping fee at the installations visited ranged from \$47.50 to \$116 per ton. At the average weight of 52 lbs. per wooden pallet, a total of 39 pallets of scrap wood would incur a tonnage landfill tipping fee. On the other hand, an installation that sells scrap wooden pallets, even

at the low price of \$0.0045 per lb. avoids the tipping fees, makes a small profit, and is credited with a cost avoidance benefit in its Annual Solid Waste Report. A total cost avoidance of \$52,500 has been claimed by the four installations visited.

Distribution of Cash Proceeds

Cash proceeds from the sale of wooden pallets were distributed in accordance with existing guidance. Specifically, the four installations visited properly followed 10 U.S.C. 2577; DoD Directive 1015.6, "Funding of Morale, Welfare, and Recreation Programs," August 3, 1984; and DoD Instruction 7000.12, "Financial Management of Morale, Welfare, and Recreational Activities," May 27, 1987, in transferring pallet sales proceeds into their Morale, Welfare, and Recreation accounts. We reviewed direct sales receipts for the sale of scrap wood. For FY 1996, the four installations had properly deposited \$4,362 in their respective Morale, Welfare, and Recreation accounts.

Summary

The four installations visited had appropriately obtained, recycled, and sold excess wooden pallets. Appropriate recycling, sales, and distribution of cash proceeds occurred because the installations had properly implemented and were in compliance with current DoD recycling policies and regulations. Therefore, this report contains no recommendations.

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Part II - Additional Information

Appendix A. Evaluation Process

Scope and Methodology

Data Gathering. We reviewed DoD policies, regulations, and financial records governing the disposal of wooden pallets. We also reviewed data on pallet usage rates, pallet procurements, and pallet disposal actions. Documents reviewed were for FYs 1995 and 1996 and the first quarter of FY 1997. We interviewed DoD item managers who manage wooden pallets, DRMO managers, and Qualified Recycling Program managers. In addition, we contacted warehouse, support operations, supply personnel, and landfill refuse center managers.

Evaluation Period and Standards. This evaluation was performed from March 6 through March 25, 1997, in accordance with standards issued and implemented by the Inspector General, DoD. Accordingly, we included tests of management controls considered necessary.

Use of Computer-Processed Data. To determine whether the DRMOs we evaluated had any of the 18 different DoD national stock numbers for pallets in inventory, we processed computer inquiries using the DRMS Automated Information System. To the extent that we reviewed the computer-processed data, the data were sufficiently reliable to be used in meeting our evaluation objectives.

Contacts During the Evaluation. We visited or contacted individuals and organizations within the DoD. Further details are available on request.

Summary of Prior Coverage. Inspector General, DoD, Report No 97-087, "Direct Sales of Recyclable Material," February 4, 1997, focused on determining whether DoD policy pertaining to the direct sale of recyclable material was followed at DoD installations with that authority. The report stated that DoD installations generally complied with existing policy regarding the conduct of direct sales, that sale proceeds were properly distributed within the Services, and that no prohibited items were sold through the direct sales program. The report recommended that improved guidance be issued to ensure that accurate financial sales transactions were properly maintained. In addition, it recommended that the reimbursable costs associated with operating a Qualified Recycling Program be specifically defined in DoD regulations, and that outsourcing opportunities be considered when a Qualified Recycling Program was established or modified to include direct sales authority. Management concurred with all recommendations and agreed to include the recommended changes in its Qualified Recycling Program Guide.

Management Control Program

Management Control Program Guidance. DoD Directive 5010.38, "Management Control Program," August 26, 1996, requires DoD organizations to implement a comprehensive system of management controls that provide reasonable assurance that programs are operating as intended, and to evaluate the adequacy of the controls.

Scope of Review of the Management Control Program. To determine whether managers had implemented management control systems that identified and corrected weaknesses, we reviewed the adequacy of management controls established for overall program oversight. Specifically, we evaluated management controls over the accountability, administration, and distribution of sales proceeds related to processes for obtaining and recycling pallets.

Adequacy of Management Controls. The management controls reviewed were adequate in that we identified no material management control weaknesses.

Appendix B. Allegations and Responses

Allegation 1. Installations were not recycling pallets through Defense Reutilization and Marketing Offices.

Response. The allegation was substantiated. However, this complies with Headquarters, DRMS policy. Further, DoD Manual 4160.21-M, "Defense Reutilization and Marketing Manual," March 1990, chapter VI, section D, paragraph D.2.c. states, "The DRMO may not accept . . . refuse and trash." The pallets that DRMOs receive are considered disposal refuse because in most cases, the pallets are unserviceable or damaged beyond economic repair.

Allegation 2. Installations were selling pallets without authorization to sell recyclable material.

Response. The allegation was unsubstantiated. All four installations visited were properly selling pallets in accordance with DoD Instruction 4715.4 and the combined Service memorandum, "Interim Guidance for Direct Sales."

Allegation 3. Cash proceeds were distributed to installations' Morale, Welfare, and Recreation accounts without authorization.

Response. The allegation was unsubstantiated. Installations were properly following 10 U.S.C. 2577 as amended, which states, ". . . after program costs are recovered, installations may use up to 50 percent of the net proceeds from the sale of recyclable materials for various environmental or health and safety purposes or the net proceeds may go towards Morale, Welfare, and Recreation programs." We verified that recycling cash proceeds were deposited into each installations' Morale, Welfare, and Recreation account.

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Evaluation Team Members

This report was prepared by the Logistics Support Directorate, Office of the Assistant Inspector General for Auditing, DoD.

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